

General Fund Revenue Book

- Economic Forecast
- Revenue Projections
- Tax Expenditure Budget

Fiscal Year 1999



Philip E. Batt, Governor

State of Idaho
Philip E. Batt, Governor

General Fund Revenue Book

**FY 1999 Executive Budget
January 1998**

- Economic Forecast
- Revenue Projections
- Tax Structure

prepared by the Division of Financial Management

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TABLE OF CONTENTS

Introduction	1
Section 1 - Economic Forecast	3
Executive Summary.....	5
National Forecast Description.....	8
Idaho Forecast Description.....	13
Alternative Forecasts.....	18
Section 2 - Revenue Projections	21
Description of Individual Revenue Sources	21
General Fund Revenue Summary.....	22
Individual Income Tax.....	24
Corporate Income Tax.....	26
Sales Tax	28
Cigarette Tax	30
Beer Tax	32
Wine Tax.....	34
Liquor Surcharge.....	36
Kilowatt-Hour Tax	37
Mine License Tax.....	38
State Treasurer	39
Judicial Branch.....	39
Department of Insurance.....	40
Department of Law Enforcement	41
Unclaimed Property.....	41
Other Departments and Transfers.....	42
Miscellaneous Revenues.....	43
Section 3 - Tax Structure	45
Introduction	47
Individual and Corporate Income Tax.....	49
Sales and Use Tax.....	51
Fiscal Summary Table.....	54
Tax Structure Detail	57
Individual and Corporate Income Tax.....	57
Sales and Use Tax.....	64
Cross Reference Table.....	77
In <i>General Fund Revenue Book Order</i>	77
In <i>Idaho Code Order</i>	80

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INTRODUCTION

The basis for most of the revenue projections made in this book is the *Idaho Economic Forecast* published by the Division of Financial Management (DFM), which in turn is based on the Idaho Economic Model (IEM). Each major revenue category (personal income tax, sales tax, and corporate income tax) is specified as a function of relevant explanatory variables.

Although the revenue model is specified in precise quantitative terms, two levels of uncertainty exist. The first of these uncertainties is associated with the statistical process itself and hence may be reduced to probabilities and confidence intervals. The other is related to the uncertainties associated with unknown future events. Weather effects on agriculture are a classic example. A forecast of agricultural production must either assume average weather or project some specific future weather condition. The forecast is contingent upon that assumed weather pattern actually occurring. Some other weather pattern will result in a different outcome for both farmers and the myriad of entities dependent upon the fortunes of farmers.

The contingent nature of an agricultural model demonstrates the uncertainty associated with any model containing exogenous variables. Both sources of forecast error are present in any model that is dependent on explanatory variables. Since most of Idaho's revenue sectors depend heavily on Idaho income levels, the revenue forecast is particularly sensitive to those factors that influence Idaho's income.

The major foundation of the IEM is economic base theory. Idaho's economy can be divided into "basic" and "domestic" activities (also known as "export" and "residential"). The basic activities, such as agriculture, forestry, mining, manufacturing, tourism, and exported services are characterized by a major dependence on external forces; while domestic activities like construction, trade, local services, and public utilities are characterized by a dependence on influences from within the state. The idea is that basic activities form the foundation of Idaho's level of economic activity, while domestic activities essentially follow from basic activities. While not a perfect theory, economic base theory does serve as a useful means of identifying the driving forces behind Idaho's overall level of economic activity.

¹ The IEM is in turn based on the Standard and Poor's DRI (DRI) Quarterly Model of the U.S. Economy. Descriptions of both are available in the current *Idaho Economic Forecast*, Division of Financial Management.